

Vera Bradley, Inc.  
Form 10-Q  
December 10, 2014  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the Quarterly Period Ended November 1, 2014  
OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the Transition Period From \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number: 001-34918

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VERA BRADLEY, INC.  
(Exact name of registrant as specified in its charter)

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Indiana 27-2935063  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

12420 Stonebridge Road, 46783  
Roanoke, Indiana  
(Address of principal executive offices) (Zip Code)

(877) 708-8372  
(Registrant's telephone number, including area code)

None  
(Former name, former address and former fiscal year, if changed since last report)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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Large accelerated filer      ☐      Accelerated filer      ☒

Non-accelerated filer      ☐ (Do not check if a smaller reporting company)      Smaller reporting company      ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).    Yes ☐    No ☒

The registrant had 40,308,621 shares of its common stock outstanding as of December 10, 2014.

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**FORWARD-LOOKING STATEMENTS**

This report contains forward-looking statements that are subject to risks and uncertainties. All statements other than statements of historical or current fact included in this report are forward-looking statements. Forward-looking statements refer to our current expectations and projections relating to our financial condition, results of operations, plans, objectives, strategies, future performance, and business. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as “anticipate,” “estimate,” “expect,” “project,” “plan,” “intend,” “believe,” “may,” “might,” “will,” “should,” “can have,” and “li” words and terms of similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. For example, all statements we make relating to our estimated and projected earnings, revenues, costs, expenditures, cash flows, growth rates, and financial results, our plans and objectives for future operations, growth, initiatives, or strategies, or the expected outcome or impact of pending or threatened litigation are forward-looking statements. All forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those that we expected, including:

- possible adverse changes in general economic conditions and their impact on consumer confidence and consumer spending;
- possible inability to predict and respond in a timely manner to changes in consumer demand;
- possible loss of key management or design associates or inability to attract and retain the talent required for our business;
- possible inability to maintain and enhance our brand;
- possible inability to successfully implement our growth strategies or manage our growing business;
- possible inability to successfully open and operate new stores as planned;
- possible adverse changes in the cost of raw materials and labor used to manufacture our products; and
- possible adverse effects resulting from a significant disruption in our single distribution facility.

We derive many of our forward-looking statements from our operating plans and forecasts, which are based upon detailed assumptions. While we believe that our assumptions are reasonable, we caution that it is difficult to predict the impact of known factors, and it is impossible for us to anticipate all factors that could affect our actual results. For a discussion of these risks and other risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the fiscal year ended February 1, 2014, as well as Item 1A of Part II of this Quarterly Report on Form 10-Q.

We caution you that the risks and uncertainties identified by us may not be all of the factors that are important to you. Furthermore, the forward-looking statements included in this report are made only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events, or otherwise, except as required by law.

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Vera Bradley, Inc.  
Consolidated Balance Sheets  
(in thousands)  
(unaudited)

|   | November 1,<br>2014 | February 1,<br>2014 |
|---|---------------------|---------------------|
| Assets  |                     |                     |
| Current assets:   |                     |                     |
| Cash and cash equivalents   | \$90,334            | \$59,215            |
| Accounts receivable, net  | 38,136              | 29,174              |
| Inventories   | 106,256             | 136,923             |
| Income taxes receivable   | 2,717               | —                   |
| Prepaid expenses and other current assets   | 9,303               | 9,952               |
| Deferred income taxes   | 15,297              | 13,094              |
| Total current assets  | 262,043             | 248,358             |
| Property, plant, and equipment, net   | 103,567             | 84,940              |
| Other assets  | 614                 | 1,085               |
| Total assets  | \$366,224           | \$334,383           |
| Liabilities and Shareholders' Equity  |                     |                     |
| Current liabilities:  |                     |                     |
| Accounts payable  | \$28,511            | \$27,745            |
| Accrued employment costs  | 14,039              | 10,586              |
| Other accrued liabilities   | 17,699              | 14,891              |
| Income taxes payable  | 2,592               | 1,625               |
| Total current liabilities   | 62,841              | 54,847              |
| Deferred income taxes   | 3,323               | 4,643               |
| Other long-term liabilities   | 24,010              | 19,746              |
| Total liabilities   | 90,174              | 79,236              |
| Commitments and contingencies   |                     |                     |
| Shareholders' equity:   |                     |                     |
| Preferred stock; 5,000 shares authorized, no shares issued or outstanding   | —                   | —                   |
| Common stock, without par value; 200,000 shares authorized, 40,689 and 40,607 shares issued and 40,520 and 40,607 outstanding, respectively | —                   | —                   |
| Additional paid-in-capital  | 80,488              | 78,153              |
| Retained earnings   | 199,108             | 178,002             |
| Accumulated other comprehensive loss  | (13                 | ) (1,008            |
| Treasury stock  | (3,533              | ) —                 |
| Total shareholders' equity  | 276,050             | 255,147             |
| Total liabilities and shareholders' equity  | \$366,224           | \$334,383           |
| The accompanying notes are an integral part of these financial statements.  |                     |                     |

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Vera Bradley, Inc.  
Consolidated Statements of Income  
(in thousands, except per share data)  
(unaudited)

|   | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|---|----------------------|---------------------|-------------------------|---------------------|
|   | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Net revenues  | \$125,204            | \$128,949           | \$356,361               | \$374,477           |
| Cost of sales   | 59,436               | 57,710              | 167,394                 | 164,900             |
| Gross profit  | 65,768               | 71,239              | 188,967                 | 209,577             |
| Selling, general, and administrative expenses         | 53,274               | 47,565              | 153,982                 | 148,691             |
| Other income  | 1,110                | 1,027               | 3,152                   | 3,608               |
| Operating income                                      | 13,604               | 24,701              | 38,137                  | 64,494              |
| Interest expense, net                                 | 215                  | 139                 | 319                     | 470                 |
| Income from continuing operations before income taxes | 13,389               | 24,562              | 37,818                  | 64,024              |
| Income tax expense                                    | 4,668                | 8,905               | 14,326                  | 23,799              |
| Income from continuing operations                     | 8,721                | 15,657              | 23,492                  | 40,225              |
| Loss from discontinued operations, net of taxes       | (1,780)              | (431)               | (2,386)                 | (859)               |
| Net income  | \$6,941              | \$15,226            | \$21,106                | \$39,366            |
| Basic weighted-average shares outstanding             | 40,663               | 40,605              | 40,663                  | 40,596              |
| Diluted weighted-average shares outstanding           | 40,716               | 40,652              | 40,720                  | 40,633              |
| Net income (loss) per share - basic                   |                      |                     |                         |                     |
| Continuing operations                                 | \$0.21               | \$0.39              | \$0.58                  | \$0.99              |
| Discontinued operations                               | (0.04)               | (0.01)              | (0.06)                  | (0.02)              |
| Net income  | \$0.17               | \$0.37              | \$0.52                  | \$0.97              |
| Net income (loss) per share - diluted                 |                      |                     |                         |                     |
| Continuing operations                                 | \$0.21               | \$0.39              | \$0.58                  | \$0.99              |
| Discontinued operations                               | (0.04)               | (0.01)              | (0.06)                  | (0.02)              |
| Net income  | \$0.17               | \$0.37              | \$0.52                  | \$0.97              |

The accompanying notes are an integral part of these financial statements.

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Vera Bradley, Inc.  
 Consolidated Statements of Comprehensive Income  
 (in thousands)  
 (unaudited)

|                                   | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|-----------------------------------|----------------------|---------------------|-------------------------|---------------------|
|                                   | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Net income                        | \$6,941              | \$15,226            | \$21,106                | \$39,366            |
| Cumulative translation adjustment | 3                    | 47                  | (1                      | ) (234              |
| Comprehensive income              | \$6,944              | \$15,273            | \$21,105                | \$39,132            |

The accompanying notes are an integral part of these financial statements.

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Vera Bradley, Inc.  
Consolidated Statements of Cash Flows  
(in thousands)  
(unaudited)

|   | Thirty-Nine Weeks Ended |                     |
|---|-------------------------|---------------------|
|   | November 1,<br>2014     | November 2,<br>2013 |
| Cash flows from operating activities  |                         |                     |
| Net income  | \$21,106                | \$39,366            |
| Adjustments to reconcile net income to net cash provided by operating activities: |                         |                     |
| Depreciation of property, plant, and equipment                                    | 10,957                  | 10,651              |
| Provision for doubtful accounts   | (129)                   | (190)               |
| Loss on disposal of property, plant, and equipment                                | —                       | 9                   |
| Stock-based compensation  | 2,943                   | 2,857               |
| Deferred income taxes   | (3,523)                 | (624)               |
| Changes in assets and liabilities:  |                         |                     |
| Accounts receivable   | (8,833)                 | (7,921)             |
| Inventories   | 30,667                  | (19,154)            |
| Prepaid expenses and other assets   | 1,120                   | 1,531               |
| Accounts payable  | (6,901)                 | 12,742              |
| Income taxes payable  | (1,750)                 | (8,726)             |
| Accrued and other liabilities   | 10,596                  | 4,305               |
| Net cash provided by operating activities   | 56,253                  | 34,846              |
| Cash flows from investing activities  |                         |                     |
| Purchases of property, plant, and equipment                                       | (22,358)                | (15,418)            |
| Net cash used in investing activities   | (22,358)                | (15,418)            |
| Cash flows from financing activities  |                         |                     |
| Payments on financial-institution debt  | —                       | (45,000)            |
| Borrowings on financial-institution debt  | —                       | 30,000              |
| Tax withholdings for equity compensation  | (608)                   | (411)               |
| Repurchase of common stock  | (3,092)                 | —                   |
| Other financing activities, net   | (71)                    | 122                 |
| Net cash used in financing activities   | (3,771)                 | (15,289)            |
| Effect of exchange rate changes on cash and cash equivalents                      | 995                     | (30)                |
| Net increase in cash and cash equivalents   | 31,119                  | 4,109               |
| Cash and cash equivalents, beginning of period                                    | 59,215                  | 9,603               |
| Cash and cash equivalents, end of period  | \$90,334                | \$13,712            |
| Supplemental disclosure of cash flow information                                  |                         |                     |
| Non-cash operating, investing, and financing activities                           |                         |                     |
| Repurchase of common stock incurred but not yet paid                              | \$441                   | \$—                 |
| Property, plant, and equipment expenditures incurred but not yet paid             | \$7,226                 | \$—                 |
| The accompanying notes are an integral part of these financial statements.        |                         |                     |



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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements  
(unaudited)

1. Description of the Company and Basis of Presentation

The terms “Company” and “Vera Bradley” refer to Vera Bradley, Inc. and its subsidiaries, except where context requires or where otherwise indicated.

Vera Bradley is a leading designer of women’s handbags and accessories, luggage and travel items, eyewear, and stationery and gifts. Founded in 1982 by friends Barbara Bradley Baekgaard and Patricia R. Miller, the brand’s iconic designs and versatile styles offer women of all ages a colorful way to accessorize every look.

Vera Bradley offers a unique, multi-channel sales model, as well as a focus on service and a high level of customer engagement. The Company sells its products through two reportable segments: Direct and Indirect. The Direct business consists of sales of Vera Bradley products through the Company’s full-line and factory outlet stores in the United States, verabradley.com, direct-to-consumer eBay sales, and the Company’s annual outlet sale in Fort Wayne, Indiana. As of November 1, 2014, the Company operated 95 full-line stores and 27 factory outlet stores. The Indirect business consists of sales of Vera Bradley products to approximately 2,850 specialty retail doors, substantially all of which are located in the United States, as well as department stores, national accounts, third party e-commerce sites, the Company’s wholesale business in Japan, and third party inventory liquidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”). Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) have been omitted. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the fiscal year ended February 1, 2014, filed with the SEC.

The interim financial statements reflect all adjustments that are, in the opinion of management, necessary to present fairly the results for the interim periods presented. All such adjustments are of a normal, recurring nature. The results of operations for the thirteen and thirty-nine weeks ended November 1, 2014, are not necessarily indicative of the results to be expected for the full fiscal year.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. The Company has eliminated intercompany balances and transactions in consolidation.

Fiscal Periods

The Company’s fiscal year ends on the Saturday closest to January 31. References to the fiscal quarters ended November 1, 2014, and November 2, 2013, refer to the thirteen-week periods ended on those dates.

Operating Leases and Tenant-Improvement Allowances

The Company has leases that contain rent holidays and predetermined, fixed escalations of minimum rentals. For each of these leases, the Company recognizes the related rent expense on a straight-line basis commencing on the date of initial possession of the leased property. The Company records the difference between the recognized rent expense and the amount payable under the lease as a deferred rent liability. As of November 1, 2014 and February 1, 2014, deferred rent liability was \$8.6 million and \$7.0 million, respectively, and is included within other long-term liabilities on the Consolidated Balance Sheets.

The Company receives tenant-improvement allowances from some of the landlords of its leased properties. These allowances generally are in the form of cash received by the Company from its landlords as part of the negotiated lease terms. The Company records each tenant-improvement allowance as a deferred credit and amortizes the allowance on a straight-line basis as a reduction to rent expense over the term of the lease, commencing on the possession date. As of November 1, 2014 and February 1, 2014, the deferred lease credit liability was \$13.6 million

and \$10.3 million, respectively. Of these amounts, \$1.8 million and \$1.4 million is included within other accrued liabilities as of November 1, 2014 and February 1, 2014, respectively; and \$11.8 million and \$8.9 million is included within other long-term liabilities as of November 1, 2014 and February 1, 2014, respectively.

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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements  
(unaudited)

Recently Issued Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. This guidance states that the disposal of a component of an entity is to be reported in discontinued operations only if the disposal represents a strategic shift that has (or will have) a major effect on an entity’s operations and financial results. The pronouncement also requires additional disclosures regarding individually significant disposals of components that do not meet the criteria to be recognized as a discontinued operation as well as additional and expanded disclosures. The guidance is effective for all disposals (or classifications as held for sale) of components of an entity and all businesses or nonprofit activities that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015; it is applied prospectively. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. The Company does not expect this standard to have a material impact on the Company’s consolidated financial statements upon adoption.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. This guidance requires companies to recognize revenue in a manner that depicts the transfer of promised goods or services to customers in amounts that reflect the consideration to which a company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. This guidance will be effective beginning in fiscal 2017, and early adoption is not permitted. The standard allows for either a full retrospective or a modified retrospective transition method. The Company is currently evaluating the impact of this standard, including the transition method, on its consolidated results of operations, financial position and cash flows. The Company does not expect the adoption of this standard to have a material impact on the Company’s consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern which requires management to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and provide related footnote disclosures. The guidance is effective for annual or interim reporting periods beginning on or after December 15, 2016. Early adoption is permitted for financial statements that have not been previously issued. The standard allows for either a full retrospective or modified retrospective transition method. The Company does not expect this standard to have an impact on the Company’s consolidated financial statements upon adoption.

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## 2. Earnings Per Share

Basic earnings per share is computed based on the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed based on the weighted-average number of common shares outstanding, plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares represent outstanding restricted stock units. The components of basic and diluted earnings per share were as follows (in thousands, except per share data):

|  | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|--|----------------------|---------------------|-------------------------|---------------------|
|  | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Numerator:   |                      |                     |                         |                     |
| Income from continuing operations                  | \$8,721              | \$15,657            | \$23,492                | \$40,225            |
| Loss from discontinued operations, net of taxes    | (1,780)              | (431)               | (2,386)                 | (859)               |
| Net income   | \$6,941              | \$15,226            | \$21,106                | \$39,366            |
| Denominator:                                       |                      |                     |                         |                     |
| Weighted-average number of common shares (basic)   | 40,663               | 40,605              | 40,663                  | 40,596              |
| Dilutive effect of stock-based awards              | 53                   | 47                  | 57                      | 37                  |
| Weighted-average number of common shares (diluted) | 40,716               | 40,652              | 40,720                  | 40,633              |
| Earnings per share - basic:                        |                      |                     |                         |                     |
| Continuing operations                              | \$0.21               | \$0.39              | \$0.58                  | \$0.99              |
| Discontinued operations                            | (0.04)               | (0.01)              | (0.06)                  | (0.02)              |
| Net income   | \$0.17               | \$0.37              | \$0.52                  | \$0.97              |
| Earnings per share - diluted:                      |                      |                     |                         |                     |
| Continuing operations                              | \$0.21               | \$0.39              | \$0.58                  | \$0.99              |
| Discontinued operations                            | (0.04)               | (0.01)              | (0.06)                  | (0.02)              |
| Net income   | \$0.17               | \$0.37              | \$0.52                  | \$0.97              |

As of November 1, 2014 and November 2, 2013, there were an immaterial number of additional shares issuable upon the vesting of restricted stock units that were excluded from the diluted share calculations because they were anti-dilutive.

## 3. Fair Value of Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Assets and liabilities measured at fair value are classified using the following hierarchy, which is based upon the transparency of inputs to the valuation as of the measurement date:

Level 1 – Quoted prices in active markets for identical assets or liabilities;

Level 2 – Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly;

Level 3 – Unobservable inputs based on the Company's own assumptions.

The classification of fair value measurements within the hierarchy is based upon the lowest level of input that is significant to the measurement.

The carrying amounts reflected on the Consolidated Balance Sheets for cash and cash equivalents, receivables, other current assets, and payables as of November 1, 2014, and February 1, 2014, approximated their fair values.

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## 4. Inventories

The components of inventories were as follows (in thousands):

|                   | November 1,<br>2014 | February 1,<br>2014 |
|-------------------|---------------------|---------------------|
| Raw materials     | \$8,471             | \$10,772            |
| Work in process   | 514                 | 850                 |
| Finished goods    | 97,271              | 125,301             |
| Total inventories | \$106,256           | \$136,923           |

## 5. Debt

As of November 1, 2014 and February 1, 2014, the Company had borrowing availability of \$125.0 million under the amended and restated credit agreement.

## 6. Income Taxes

The provision for income taxes for interim periods is based on an estimate of the annual effective tax rate adjusted to reflect the impact of discrete items. Management judgment is required in projecting ordinary income to estimate the Company's annual effective tax rate.

The effective tax rate for the thirteen weeks ended November 1, 2014, was 34.9%, compared to 36.3% for the thirteen weeks ended November 2, 2013. The year-over-year decrease is primarily due to state tax matters, including the reversal of FIN48 reserves, partially offset by the effect of non-deductible items becoming a larger percentage of income from continuing operations before income taxes.

The effective tax rate for the thirty-nine weeks ended November 1, 2014, was 37.9%, compared to 37.2% for the thirty-nine weeks ended November 2, 2013. The year-over-year increase is primarily due to the effect of non-deductible items becoming a larger percentage of income from continuing operations before income taxes, partially offset by state tax matters including a net reduction in FIN48 reserves.

## 7. Stock-Based Compensation

The Company recognizes share-based compensation expense, for its awards of restricted stock and restricted stock units, in an amount equal to the fair market value of the underlying stock on the grant date of the respective award. The Company reserved 6,076,001 shares of common stock for issuance or transfer under the 2010 Equity and Incentive Plan, which allows for grants of restricted stock units, as well as other equity awards.

## Awards of Restricted Stock Units

During the thirteen weeks ended November 1, 2014, the Company granted 2,500 time-based restricted stock units with an aggregate fair value of \$0.1 million to certain employees under the 2010 Equity and Incentive Plan compared to a total of 2,546 time-based restricted stock units with an aggregate fair value of \$0.1 million granted in the same period of the prior year.

During the thirty-nine weeks ended November 1, 2014, the Company granted 280,991 time-based and performance-based restricted stock units with an aggregate fair value of \$7.4 million to certain employees and non-employee directors under the 2010 Equity and Incentive Plan compared to a total of 247,360 time-based and performance-based restricted stock units with an aggregate fair value of \$5.8 million granted in the same period of the prior year. The Company determined the fair value of the awards based on the closing price of the Company's common stock on the grant date.

The majority of time-based restricted stock units vest and settle in shares of the Company's common stock, on a one-for-one basis, in equal installments on each of the first three anniversaries of the grant date. Beginning in fiscal 2014, all restricted stock units issued to non-employee directors vest after a one-year period from grant date. The Company is recognizing the expense relating to these units, net of estimated forfeitures, on a straight-line basis over the vesting period.



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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements

(unaudited)

Performance-based restricted stock units vest upon the completion of a three-year period of time (cliff vesting), subject to the employee's continuing employment throughout the three-year performance period and the Company's achievement of annual net income or earnings per share targets during the three-year performance period. The Company is recognizing the expense relating to these units, net of estimated forfeitures, based on the probable outcome of achievement of the financial targets, on a straight-line basis over three years.

The following table sets forth a summary of restricted stock unit activity for the period ended November 1, 2014 (units in thousands):

|   | Time-based<br>Restricted Stock Units |   | Performance-based<br>Restricted Stock Units |   |
|---|--------------------------------------|---|---|---|
|   | Number of<br>Units                   | Weighted-<br>Average<br>Grant<br>Date Fair<br>Value<br>(per unit) | Number of<br>Units                          | Weighted-<br>Average<br>Grant<br>Date Fair<br>Value<br>(per unit) |
| Nonvested units outstanding at February 1, 2014 | 231                                  | \$26.92   | 160   | \$25.75   |
| Granted   | 169                                  | 25.71   | 112   | 26.94   |
| Vested  | (105)                                | ) 27.05   | —   | —   |
| Forfeited                                       | (37)                                 | ) 25.91   | (46)  | ) 26.08   |
| Nonvested units outstanding at November 1, 2014 | 258                                  | \$26.22   | 226   | \$26.27   |

As of November 1, 2014, there was \$6.4 million of total unrecognized compensation cost, net of estimated forfeitures, related to nonvested restricted stock units. That cost is expected to be recognized over a weighted-average period of 1.8 years.

#### 8. Commitments and Contingencies

The Company is subject to various claims and contingencies arising in the normal course of business, including those relating to product liability, legal, employee benefit, environmental, and other matters. Management believes that it is not reasonably possible that any of these claims will have a material adverse effect on the Company's financial condition, results of operations, or cash flows.

#### 9. Segment Reporting

The Company has two operating segments, which are also its reportable segments: Direct and Indirect. These operating segments are components of the Company for which separate financial information is available and for which operating results are evaluated on a regular basis by the chief operating decision maker in deciding how to allocate resources and in assessing the performance of the segments.

The Direct segment includes the Company's full-line and factory outlet stores, the Company's website, verabradley.com, direct-to-consumer eBay sales, and the annual outlet sale. Revenues generated through this segment are driven through the sale of Company-branded products from Vera Bradley to end consumers. The Company exited its direct Japan operations in the third quarter. Direct segment results for the current and prior periods presented are reported on a continuing operations basis unless otherwise stated. Discontinued operations are detailed in Note 11 Discontinued Operations of this Quarterly Report on Form 10-Q.

The Indirect segment represents revenues generated through the distribution of Company-branded products to specialty retailers representing approximately 2,850 doors, substantially all of which are located in the United States,

as well as key accounts, which include department stores, national accounts, third party e-commerce sites, the Company's wholesale business in Japan, and third party inventory liquidation.

Corporate costs represent the Company's administrative expenses, which include, but are not limited to: human resources, legal, finance, information technology, design, merchandising, and various other corporate-level-activity-related expenses. All intercompany-related activities are eliminated in consolidation and are excluded from the segment reporting.



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Vera Bradley, Inc.  
Notes to the Consolidated Financial Statements  
(unaudited)

Company management evaluates segment operating results based on several indicators. The primary or key performance indicators for each segment are net revenues and operating income. Net revenues and operating income information for the Company's reportable segments consisted of the following (in thousands):

|                                | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|--------------------------------|----------------------|---------------------|-------------------------|---------------------|
|                                | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Segment net revenues:          |                      |                     |                         |                     |
| Direct                         | \$77,946             | \$67,712            | \$227,907               | \$213,538           |
| Indirect                       | 47,258               | 61,237              | 128,454                 | 160,939             |
| Total                          | \$125,204            | \$128,949           | \$356,361               | \$374,477           |
| Segment operating income:      |                      |                     |                         |                     |
| Direct                         | \$13,863             | \$15,293            | \$44,742                | \$51,802            |
| Indirect                       | 19,204               | 25,956              | 50,590                  | 65,501              |
| Total                          | \$33,067             | \$41,249            | \$95,332                | \$117,303           |
| Reconciliation:                |                      |                     |                         |                     |
| Segment operating income       | \$33,067             | \$41,249            | \$95,332                | \$117,303           |
| Less:                          |                      |                     |                         |                     |
| Unallocated corporate expenses | (19,463              | ) (16,548           | ) (57,195               | ) (52,809           |
| Operating income               | \$13,604             | \$24,701            | \$38,137                | \$64,494            |

#### 10. Common Stock

On September 9, 2014, the Company's board of directors approved a share repurchase program (the "2014 Share Repurchase Program") authorizing up to \$40.0 million of repurchases of shares of the Company's common stock. The 2014 Share Repurchase Program expires in October 2016.

The Company purchased 168,582 shares at an average price of \$20.96 per share, excluding commissions, for an aggregate amount of \$3.5 million during the thirteen and thirty-nine weeks ended November 1, 2014. As of November 1, 2014, there was \$36.5 million remaining available to repurchase shares of the Company's common stock under the 2014 Share Repurchase Program.

As of November 1, 2014, the Company held as treasury shares 168,582 shares of its common stock at an average price of \$20.96 per share, excluding commissions, for an aggregate carrying amount of \$3.5 million. The Company's treasury shares may be issued under the 2010 Equity and Incentive Plan or for other corporate purposes. Further purchases will occur from time to time as market conditions warrant and as the Company deems appropriate when judged against alternative uses of cash.

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## 11. Discontinued Operations

On June 4, 2014, the Company entered into a five-year agreement with Mitsubishi Corporation Fashion Company and Look Inc. to import and distribute Vera Bradley products in Japan. As a result of moving to this wholesale business model, the Company exited its direct business in Japan during the third quarter of fiscal 2015 and the results of operations are reported as discontinued operations. Japan results were previously reported in the Direct segment, which has been restated to exclude the results of the discontinued operations for the periods presented. Following are the Japan results of operations (in thousands):

|  | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|--|----------------------|---------------------|-------------------------|---------------------|
|  | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Net revenues   | \$555                | \$1,145             | \$2,963                 | \$4,022             |
| Cost of sales  | 447                  | 451                 | 1,470                   | 1,427               |
| Gross profit   | 108                  | 694                 | 1,493                   | 2,595               |
| Selling, general, and administrative expenses                | 618                  | 1,125               | 2,985                   | 3,454               |
| Operating loss   | (510)                | (431)               | (1,492)                 | (859)               |
| Loss on disposal from discontinued operations <sup>(1)</sup> | (1,769)              | —                   | (1,769)                 | —                   |
| Loss before income taxes                                     | (2,279)              | (431)               | (3,261)                 | (859)               |
| Income tax benefit   | (499)                | —                   | (875)                   | —                   |
| Loss from discontinued operations                            | \$(1,780)            | \$(431)             | \$(2,386)               | \$(859)             |

<sup>(1)</sup> Loss on disposal from discontinued operations primarily relates to cumulative foreign currency translation adjustments.

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion summarizes the significant factors affecting the consolidated operating results, financial condition, liquidity, and cash flows of our Company as of and for the thirteen and thirty-nine weeks ended November 1, 2014 and November 2, 2013. The following discussion should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended February 1, 2014, and our unaudited consolidated financial statements and the related notes included in Item 1 of this Quarterly Report.

#### Executive Summary

Below is a summary of our strategic progress and financial highlights:

#### Strategic Progress

- We opened six new full-line stores and seven factory outlet stores during the third quarter.
- We introduced our new coordinating collections, further intensified our solid microfiber offerings, and launched our leather and faux leather halo collections.
- We enhanced the visual presentation in our full-line stores and added a larger selection of factory exclusive products to our factory outlet stores.
- We made key enhancements to verabradley.com, including adding product recommendations, enhancing product descriptions, adding silhouettes for product scale, generating cart and site abandonment emails, and gathering and analyzing customer feedback.
- We launched our first national advertising campaign focused on leather and faux leather in September.

#### Financial Summary

- Net revenues decreased 2.9% to \$125.2 million.
- Direct segment sales increased 15.1% to \$77.9 million. Comparable sales (including e-commerce) increased 0.9%.
- Indirect segment sales decreased 22.8% to \$47.3 million.
- Gross profit was \$65.8 million (52.5% of net revenue).
- Operating income was \$13.6 million (10.9% of net revenue).
- Income from continuing operations was \$8.7 million, or \$0.21 per diluted share.
- Cash and cash equivalents were \$90.3 million at November 1, 2014.
- Capital expenditures for the thirty-nine weeks totaled \$22.4 million, which were funded from cash generated from operations of \$56.3 million.

In June 2014, we entered into a five-year agreement with Mitsubishi Corporation Fashion Company and Look Inc. to import and distribute Vera Bradley products in Japan. As a result of moving to this wholesale business model, we exited our direct business in Japan during the third quarter of fiscal 2015 and are accounting for it as a discontinued operation. Consolidated income statement and Direct segment results for the current and prior periods presented are reported on a continuing operations basis unless otherwise stated.

#### How We Assess the Performance of Our Business

In assessing the performance of our business, we consider a variety of performance and financial measures.

#### Net Revenues

Net revenues reflect revenues from the sale of our merchandise and from distribution and shipping and handling fees, less returns and discounts. Revenues for the Direct segment reflect sales through our full-line and factory outlet stores, verabradley.com, direct-to-consumer eBay sales, and our annual outlet sale in Fort Wayne, Indiana. Revenues for the Indirect segment reflect sales to specialty retail partners, department stores, national accounts, third party e-commerce sites, our wholesale business in Japan, and third party inventory liquidation.

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### Comparable Sales

Comparable sales (including e-commerce) are calculated based upon our stores that have been open for at least 12 full fiscal months and net revenues from our e-commerce operations. Comparable store sales are calculated based solely upon our stores that have been open for at least 12 full fiscal months. Remodeled stores are included in comparable sales and comparable store sales unless the store was closed for a portion of the current or comparable prior period or the remodel resulted in a significant change in square footage. Some of our competitors and other retailers calculate comparable or “same store” sales differently than we do. As a result, data in this report regarding our comparable sales and comparable store sales may not be comparable to similar data made available by other companies.

Non-comparable sales include sales from stores not included in comparable sales or comparable store sales.

Measuring the change in year-over-year comparable sales allows us to evaluate how our store base and e-commerce operations are performing. Various factors affect our comparable sales, including:

- Overall economic trends;
- Consumer preferences and fashion trends;
- Competition;
- The timing of our releases of new patterns and collections;
- Changes in our product mix;
- Pricing;
- The level of customer service that we provide in stores;
- Our ability to source and distribute products efficiently;
- The number of stores we open and close in any period; and
- The timing and success of promotional and advertising efforts.

### Gross Profit

Gross profit is equal to our net revenues less our cost of sales. Cost of sales includes the direct cost of purchased and manufactured merchandise, distribution center costs, operations overhead, duty, and all inbound freight costs incurred. The components of our reported cost of sales may not be comparable to those of other retail and wholesale companies. Gross profit can be impacted by changes in volume; fluctuations in sales price; operational efficiencies, such as leveraging of fixed costs; promotional activities, such as free shipping; commodity prices, such as cotton; and labor costs.

### Selling, General, and Administrative Expenses (SG&A)

SG&A expenses include selling; advertising, marketing, and product development; and administrative. Selling expenses include Direct business expenses, such as store expenses, employee compensation, and store occupancy and supply costs, as well as Indirect business expenses consisting primarily of employee compensation and other expenses associated with sales to Indirect retailers. Advertising, marketing, and product development expenses include employee compensation, media costs, creative production expenses, marketing agency fees, new product design costs, public relations expenses, and market research expenses. A portion of our advertising expenses may be reimbursed by Indirect retailers, and such amount is classified as other income. Administrative expenses include employee compensation for corporate functions, corporate headquarters occupancy costs, consulting and software expenses, and charitable donations.

### Other Income

We support many of our Indirect retailers’ marketing efforts by distributing certain catalogs and promotional mailers to current and prospective customers. Our Indirect retailers reimburse us for a portion of the cost to produce these materials. Reimbursement received is recorded as other income. The related cost to design, produce, and distribute the catalogs and mailers is recorded as SG&A expense. Other income also includes proceeds from the sales of tickets to our annual outlet sale.

### Operating Income

Operating income is equal to gross profit less SG&A expenses plus other income. Operating income excludes interest income, interest expense, and income taxes.



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## Income from Continuing Operations

Income from continuing operations is equal to operating income less net interest expense and income taxes.

## Loss from Discontinued Operations, Net of Taxes

Loss from discontinued operations, net of taxes, is equal to the loss from the results of operations related to the direct Japan business, which was exited in the third quarter of fiscal year 2015, adjusted for the associated tax benefit.

## Net Income

Net income is equal to the sum of income from continuing operations and loss from discontinued operations, net of taxes.

## Results of Operations

The following tables summarize key components of our consolidated results of operations for the periods indicated, both in dollars and as a percentage of our net revenues (\$ in thousands):

|   | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|---|----------------------|---------------------|-------------------------|---------------------|
|   | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Statement of Income Data:                             |                      |                     |                         |                     |
| Net revenues  | \$125,204            | \$128,949           | \$356,361               | \$374,477           |
| Cost of sales   | 59,436               | 57,710              | 167,394                 | 164,900             |
| Gross profit  | 65,768               | 71,239              | 188,967                 | 209,577             |
| Selling, general, and administrative expenses         | 53,274               | 47,565              | 153,982                 | 148,691             |
| Other income  | 1,110                | 1,027               | 3,152                   | 3,608               |
| Operating income                                      | 13,604               | 24,701              | 38,137                  | 64,494              |
| Interest expense, net                                 | 215                  | 139                 | 319                     | 470                 |
| Income from continuing operations before income taxes | 13,389               | 24,562              | 37,818                  | 64,024              |
| Income tax expense                                    | 4,668                | 8,905               | 14,326                  | 23,799              |
| Income from continuing operations                     | 8,721                | 15,657              | 23,492                  | 40,225              |
| Loss from discontinued operations, net of taxes       | (1,780)              | (431)               | (2,386)                 | (859)               |
| Net income  | \$6,941              | \$15,226            | \$21,106                | \$39,366            |
| Percentage of Net Revenues:                           |                      |                     |                         |                     |
| Net revenues  | 100.0                | % 100.0             | % 100.0                 | % 100.0             |
| Cost of sales   | 47.5                 | % 44.8              | % 47.0                  | % 44.0              |
| Gross profit  | 52.5                 | % 55.2              | % 53.0                  | % 56.0              |
| Selling, general, and administrative expenses         | 42.5                 | % 36.9              | % 43.2                  | % 39.7              |
| Other income  | 0.9                  | % 0.8               | % 0.9                   | % 1.0               |
| Operating income                                      | 10.9                 | % 19.2              | % 10.7                  | % 17.2              |
| Interest expense, net                                 | 0.2                  | % 0.1               | % 0.1                   | % 0.1               |
| Income from continuing operations before income taxes | 10.7                 | % 19.0              | % 10.6                  | % 17.1              |
| Income tax expense                                    | 3.7                  | % 6.9               | % 4.0                   | % 6.4               |
| Income from continuing operations                     | 7.0                  | % 12.1              | % 6.6                   | % 10.7              |
| Loss from discontinued operations, net of taxes       | (1.4)                | )% (0.3             | )% (0.7                 | )% (0.2             |
| Net income  | 5.5                  | % 11.8              | % 5.9                   | % 10.5              |

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The following tables present net revenues and operating income by operating segment, both in dollars and as a percentage of our net revenues, and store data for the periods indicated (\$ in thousands, except as otherwise indicated):

|  | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|--|----------------------|---------------------|-------------------------|---------------------|
|  | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Net Revenues by Segment:   |                      |                     |                         |                     |
| Direct   | \$77,946             | \$67,712            | \$227,907               | \$213,538           |
| Indirect   | 47,258               | 61,237              | 128,454                 | 160,939             |
| Total  | \$125,204            | \$128,949           | \$356,361               | \$374,477           |
| Percentage of Net Revenues by Segment:                                     |                      |                     |                         |                     |
| Direct   | 62.3                 | % 52.5              | % 64.0                  | % 57.0              |
| Indirect   | 37.7                 | % 47.5              | % 36.0                  | % 43.0              |
| Total  | 100.0                | % 100.0             | % 100.0                 | % 100.0             |
|  | Thirteen Weeks Ended |                     | Thirty-Nine Weeks Ended |                     |
|  | November 1,<br>2014  | November 2,<br>2013 | November 1,<br>2014     | November 2,<br>2013 |
| Operating Income by Segment:   |                      |                     |                         |                     |
| Direct   | \$13,863             | \$15,293            | \$44,742                | \$51,802            |
| Indirect   | 19,204               | 25,956              | 50,590                  | 65,501              |
| Less: Corporate unallocated  | (19,463 )            | (16,548 )           | (57,195 )               | (52,809 )           |
| Total  | \$13,604             | \$24,701            | \$38,137                | \$64,494            |
| Operating Income as a Percentage of Net Revenues by Segment:               |                      |                     |                         |                     |
| Direct   | 17.8                 | % 22.6              | % 19.6                  | % 24.3              |
| Indirect   | 40.6                 | % 42.4              | % 39.4                  | % 40.7              |
| Store Data <sup>(1)</sup> :  |                      |                     |                         |                     |
| Total stores open at end of period   | 122                  | 99                  | 122                     | 99                  |
| Comparable sales (including e-commerce) increase (decrease) <sup>(2)</sup> | 0.9                  | % (5.0 )            | % (4.0 )                | % 0.6               |
| Total gross square footage at end of period (all stores)                   | 269,051              | 207,096             | 269,051                 | 207,096             |
| Average net revenues per gross square foot <sup>(3)</sup>                  | \$173                | \$212               | \$552                   | \$688               |

(1) Includes our full-line and factory outlet stores.

Comparable sales (including e-commerce) are calculated based upon our stores that have been open for at least 12 full fiscal months and net revenues from our e-commerce operations. Increase or decrease is reported as a

(2) percentage of the comparable sales for the same period in the prior fiscal year. Remodeled stores are included in comparable sales unless the store was closed for a portion of the current or comparable prior period or the remodel resulted in a significant change in square footage.

Dollars not in thousands. Average net revenues per gross square foot are calculated by dividing total net revenues

(3) for our stores that have been open at least 12 full fiscal months as of the end of the period by total gross square footage for those stores. Remodeled stores are included in average net revenues per gross square foot unless the store was closed for a portion of the period.

Thirteen Weeks Ended November 1, 2014, Compared to Thirteen Weeks Ended November 2, 2013

Net Revenues

For the thirteen weeks ended November 1, 2014, net revenues decreased \$3.7 million, or 2.9%, to \$125.2 million, from \$128.9 million in the comparable prior-year period.

Direct. For the thirteen weeks ended November 1, 2014, net revenues in the Direct segment increased \$10.2 million, or 15.1%, to \$77.9 million, from \$67.7 million in the comparable prior-year period. This change resulted from a \$9.6 million increase in revenues at our non-comparable stores which included 23 additional full-line and factory outlet stores along with a comparable



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sales (including e-commerce) increase of \$0.6 million, or 0.9% (which includes a 22.2% increase in e-commerce sales). Our comparable store sales decreased 13.5%. Comparable sales (including e-commerce) were negatively impacted by year-over-year declines in store traffic. The aggregate number of full-line and factory outlet stores grew from 99 at November 2, 2013, to 122 at November 1, 2014.

Indirect. For the thirteen weeks ended November 1, 2014, net revenues in the Indirect segment decreased \$13.9 million, or 22.8%, to \$47.3 million, from \$61.2 million in the comparable prior-year period, primarily due to lower orders from the Company's specialty retail partners, as well as a reduction in retail partner accounts.

### Gross Profit

For the thirteen weeks ended November 1, 2014, gross profit decreased \$5.4 million, or 7.7%, to \$65.8 million, from \$71.2 million in the comparable prior-year period. As a percentage of net revenues, gross profit decreased to 52.5% for the thirteen weeks ended November 1, 2014, from 55.2% in the comparable prior-year period. The decrease as a percentage of net revenues was primarily due to deleveraging of overhead costs as well as modestly increased year-over-year online promotional activity.

### Selling, General, and Administrative Expenses

For the thirteen weeks ended November 1, 2014, SG&A expenses increased \$5.7 million, or 12.0%, to \$53.3 million, from \$47.6 million in the comparable prior-year period. As a percentage of net revenues, SG&A expenses increased to 42.5% for the thirteen weeks ended November 1, 2014, from 36.9% in the comparable prior-year period. The increase in SG&A expenses as a percentage of net revenues was primarily due to strategic investments, including new store expenses, key management additions, and marketing and e-commerce initiatives.

### Other Income

For the thirteen weeks ended November 1, 2014, other income increased \$0.1 million, or 8.1%, to \$1.1 million, from \$1.0 million in the comparable prior-year period due to an increase in reimbursement of co-op mailers from Indirect retailers.

### Operating Income

For the thirteen weeks ended November 1, 2014, operating income decreased \$11.1 million, or 44.9%, to \$13.6 million, from \$24.7 million in the comparable prior-year period. As a percentage of net revenues, operating income was 10.9% and 19.2% for the thirteen weeks ended November 1, 2014 and November 2, 2013, respectively.

Direct. For the thirteen weeks ended November 1, 2014, operating income in the Direct segment decreased \$1.4 million, or 9.4%. As a percentage of Direct segment net revenues, operating income in the Direct segment was 17.8% and 22.6% for the thirteen weeks ended November 1, 2014 and November 2, 2013, respectively.

Indirect. For the thirteen weeks ended November 1, 2014, operating income in the Indirect segment decreased \$6.8 million, or 26.0%. As a percentage of Indirect segment net revenues, operating income in the Indirect segment was 40.6% and 42.4% for the thirteen weeks ended November 1, 2014 and November 2, 2013, respectively.

Corporate Unallocated. For the thirteen weeks ended November 1, 2014, unallocated expenses increased \$2.9 million, or 17.6%, primarily due to key management additions and marketing initiatives.

### Income Tax Expense

The effective tax rate for the thirteen weeks ended November 1, 2014, was 34.9%, compared to 36.3% for the thirteen weeks ended November 2, 2013. The year-over-year decrease is primarily due to state tax matters including the reversal of FIN48 reserves, partially offset by the effect of non-deductible items becoming a larger percentage of income from continuing operations before income taxes.

### Income from Continuing Operations

For the thirteen weeks ended November 1, 2014, income from continuing operations decreased \$7.0 million, or 44.3%, to \$8.7 million from \$15.7 million in the comparable prior-year period.

### Loss from Discontinued Operations, Net of Taxes

For the thirteen weeks ended November 1, 2014, loss from discontinued operations, net of taxes increased \$1.4 million to \$1.8 million from \$0.4 million in the comparable prior-year period, reflecting the exit of the direct Japan business in the third quarter of fiscal year 2015. The year-over-year increase is primarily due to cumulative foreign currency translation adjustments.



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### Net Income

For the thirteen weeks ended November 1, 2014, net income decreased \$8.3 million, or 54.4%, to \$6.9 million from \$15.2 million in the comparable prior-year period.

### Thirty-Nine Weeks Ended November 1, 2014, Compared to Thirty-Nine Weeks Ended November 2, 2013

#### Net Revenues

For the thirty-nine weeks ended November 1, 2014, net revenues decreased \$18.1 million, or 4.8%, to \$356.4 million, from \$374.5 million in the comparable prior-year period.

Direct. For the thirty-nine weeks ended November 1, 2014, net revenues in the Direct segment increased \$14.4 million, or 6.7%, to \$227.9 million, from \$213.5 million in the comparable prior-year period. This change resulted from a \$24.5 million increase in revenues at our non-comparable stores which included 23 additional full-line and factory outlet stores partially offset by a comparable sales (including e-commerce) decrease of \$7.9 million, or 4.0% (which includes a 10.8% increase in e-commerce sales), and a decrease in total sales at our annual outlet sale compared to the prior year. Our comparable store sales decreased 14.0%. The comparable sales (including e-commerce) decrease was primarily due to declines in traffic, underperformance of the product offering, and increased year-over-year promotional activity. The aggregate number of full-line and factory outlet stores grew from 99 at November 2, 2013, to 122 at November 1, 2014.

Indirect. For the thirty-nine weeks ended November 1, 2014, net revenues in the Indirect segment decreased \$32.4 million, or 20.2%, to \$128.5 million, from \$160.9 million in the comparable prior-year period, primarily due to lower orders from the Company's specialty retail partners, as well as a reduction in retail partner accounts.

#### Gross Profit

For the thirty-nine weeks ended November 1, 2014, gross profit decreased \$20.6 million, or 9.8%, to \$189.0 million, from \$209.6 million in the comparable prior-year period. As a percentage of net revenues, gross profit decreased to 53.0% for the thirteen weeks ended November 1, 2014, from 56.0% in the comparable prior-year period. The decrease as a percentage of net revenues was primarily due to deleveraging of overhead costs, as well as increased year-over-year promotional activity.

#### Selling, General, and Administrative Expenses

For the thirty-nine weeks ended November 1, 2014, SG&A expenses increased \$5.3 million, or 3.6%, to \$154.0 million, from \$148.7 million in the comparable prior-year period. As a percentage of net revenues, SG&A expenses increased to 43.2% for the thirty-nine weeks ended November 1, 2014, from 39.7% in the comparable prior-year period. The increase in SG&A expenses as a percentage of net revenues was primarily due to fixed expenses being spread over lower revenues in the Indirect segment, deleveraging of store operating expenses, and strategic investments which include new store expenses, key management additions and marketing and e-commerce initiatives, which were partially offset by cost containment efforts.

#### Other Income

For the thirty-nine weeks ended November 1, 2014, other income decreased \$0.4 million, or 12.6%, to \$3.2 million, from \$3.6 million in the comparable prior-year period, primarily due to a decrease in reimbursement of co-op mailers from Indirect retailers.

#### Operating Income

For the thirty-nine weeks ended November 1, 2014, operating income decreased \$26.4 million, or 40.9%, to \$38.1 million, from \$64.5 million in the comparable prior-year period. As a percentage of net revenues, operating income was 10.7% and 17.2% for the thirty-nine weeks ended November 1, 2014 and November 2, 2013, respectively.

Direct. For the thirty-nine weeks ended November 1, 2014, operating income in the Direct segment decreased \$7.1 million, or 13.6%. As a percentage of Direct segment net revenues, operating income in the Direct segment was 19.6% and 24.3% for the thirty-nine weeks ended November 1, 2014 and November 2, 2013, respectively.

Indirect. For the thirty-nine weeks ended November 1, 2014, operating income in the Indirect segment decreased \$14.9 million, or 22.8%. As a percentage of Indirect segment net revenues, operating income in the Indirect segment was 39.4% and 40.7% for the thirty-nine weeks ended November 1, 2014 and November 2, 2013, respectively.

Corporate Unallocated. For the thirty-nine weeks ended November 1, 2014, unallocated expenses increased \$4.4 million, or 8.3%, primarily due to headcount related expenses.



Table of Contents**Income Tax Expense**

The effective tax rate for the thirty-nine weeks ended November 1, 2014, was 37.9%, compared to 37.2% for the thirty-nine weeks ended November 2, 2013. The year-over-year increase is primarily due to the effect of non-deductible items becoming a larger percentage of income from continuing operations before income taxes, partially offset by state tax matters including a net reduction in FIN48 reserves.

**Income from Continuing Operations**

For the thirty-nine weeks ended November 1, 2014, income from continuing operations decreased \$16.7 million, or 41.6%, to \$23.5 million from \$40.2 million in the comparable prior-year period.

**Loss from Discontinued Operations, Net of Taxes**

For the thirty-nine weeks ended November 1, 2014, loss from discontinued operations, net of taxes increased \$1.5 million to \$2.4 million from \$0.9 million in the comparable prior-year period reflecting the exit of the direct Japan business in the third quarter of fiscal year 2015. The year-over-year increase is primarily due to cumulative foreign currency translation adjustments.

**Net Income**

For the thirty-nine weeks ended November 1, 2014, net income decreased \$18.3 million, or 46.4%, to \$21.1 million from \$39.4 million in the comparable prior-year period.

**Liquidity and Capital Resources****General**

Our primary source of liquidity is cash flow from operations. We also have access to additional liquidity, if needed, through borrowings under our \$125.0 million amended and restated credit agreement. Historically, our primary cash needs have been for merchandise inventories, payroll, store rent, capital expenditures associated with operational equipment, buildings, information technology, opening new stores, and debt repayments. The most significant components of our working capital are cash and cash equivalents, merchandise inventories, accounts receivable, accounts payable, and other current liabilities.

We believe that cash flows from operating activities and the availability of borrowings under our amended and restated credit agreement or other financing arrangements will be sufficient to meet working capital requirements, anticipated capital expenditures, share repurchases, and debt payments for the foreseeable future.

**Cash Flow Analysis**

A summary of operating, investing, and financing activities is shown in the following table (in thousands):

|   | Thirty-Nine Weeks Ended |                     |
|---|-------------------------|---------------------|
|   | November 1,<br>2014     | November 2,<br>2013 |
| Net cash provided by operating activities | \$56,253                | \$34,846            |
| Net cash used in investing activities     | (22,358)                | (15,418)            |
| Net cash used in financing activities     | (3,771)                 | (15,289)            |
| Net Cash Provided by Operating Activities |                         |                     |

Net cash provided by operating activities consists primarily of net income adjusted for non-cash items, including depreciation, amortization, deferred taxes, and stock-based compensation, the effect of changes in assets and liabilities, and tenant-improvement allowances received from landlords under our store leases.

Net cash provided by operating activities for the thirty-nine weeks ended November 1, 2014, was \$56.3 million, compared to \$34.8 million for the thirty-nine weeks ended November 2, 2013, an increase primarily due to a reduction in inventory, partially offset by a decrease in accounts payable.

**Net Cash Used in Investing Activities**

Investing activities consist primarily of capital expenditures for growth related to new store openings, buildings, operational equipment, and information technology investments.

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Net cash used in investing activities was \$22.4 million and \$15.4 million for the thirty-nine weeks ended November 1, 2014 and November 2, 2013, respectively; capital expenditures of \$7.2 million were incurred but not paid at November 1, 2014. The \$14.2 million increase in capital expenditures was due primarily to the campus consolidation project, which will expand our Roanoke, Indiana Design Center and Distribution Center allowing us to consolidate our current local facilities.

Capital expenditures for fiscal year 2015 are expected to be approximately \$40.0 million, which includes approximately \$20.0 million related to the campus consolidation.

### Net Cash Used in Financing Activities

Net cash used in financing activities was \$3.8 million for the thirty-nine weeks ended November 1, 2014 which was primarily related to purchases of shares of the Company's common stock made under the 2014 Share Repurchase Program. This compares to net cash used in financing activities of \$15.3 million for the thirty-nine weeks ended November 2, 2013 which was primarily related to net repayments under our amended and restated credit agreement.

### Amended and Restated Credit Agreement

On October 4, 2010, Vera Bradley Designs, Inc., our wholly owned subsidiary, entered into an agreement to amend and restate its credit agreement with JPMorgan Chase Bank, as administrative agent, and certain other lenders. The amended and restated credit agreement provides for a revolving credit commitment of \$125.0 million. On June 1, 2012, Vera Bradley Designs, Inc., entered into an amendment to the credit agreement that extends the maturity date from October 3, 2015, to June 1, 2017. Certain permitted indebtedness covenants were also amended. All borrowings under the amended and restated credit agreement are collateralized by substantially all of our assets. The credit agreement is also guaranteed by the Company. The credit agreement requires us to comply with various financial covenants, including a fixed charge coverage ratio of not less than 1.20 to 1.00 and a leverage ratio of not more than 3.50 to 1.00. The agreement also contains various other covenants, including restrictions on the incurrence of certain indebtedness, liens, investments, acquisitions, and asset sales. We were in compliance with these covenants as of November 1, 2014.

Borrowings under the amended and restated credit agreement bear interest at either LIBOR plus the applicable margin (ranging from 1.05% to 2.05%) or the alternate base rate (as defined in the agreement) plus the applicable margin (ranging from 0.05% to 1.05%). The applicable margin is tied to our leverage ratio. In addition, we are required to pay a quarterly facility fee (as defined in the agreement) ranging from 0.20% to 0.45% of the revolving credit commitment. As of November 1, 2014, the Company had borrowing availability of \$125.0 million under the agreement.

### Off-Balance-Sheet Arrangements

We do not have any off-balance-sheet financing or unconsolidated special-purpose entities.

### Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, as well as the related disclosures of contingent assets and liabilities at the date of the financial statements. A summary of the Company's significant accounting policies is included in Note 2 to the Company's consolidated financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2014.

Certain accounting policies and estimates of the Company are considered critical, as these policies and estimates are the most important to the depiction of the Company's consolidated financial statements and require significant, difficult, or complex judgments, often about the effect of matters that are inherently uncertain. Such policies are summarized in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2014. As of November 1, 2014, there was no significant change to any of the critical accounting policies and estimates described in the Annual Report.

### Recently Issued Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. This guidance states that the disposal of a component of an entity is to be reported in discontinued operations only if the disposal

represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results. The pronouncement also requires additional disclosures regarding individually significant disposals of components that do not meet the criteria to be recognized as a discontinued operation as well as additional and expanded disclosures. The guidance is effective for all disposals (or

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classifications as held for sale) of components of an entity and all businesses or nonprofit activities that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015; it is applied prospectively. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. The Company does not expect this standard to have a material impact on the Company's consolidated financial statements upon adoption.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. This guidance requires companies to recognize revenue in a manner that depicts the transfer of promised goods or services to customers in amounts that reflect the consideration to which a company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. This guidance will be effective beginning in fiscal 2017, and early adoption is not permitted. The standard allows for either a full retrospective or a modified retrospective transition method. The Company is currently evaluating the impact of this standard, including the transition method, on its consolidated results of operations, financial position and cash flows. The Company does not expect the adoption of this standard to have a material impact on the Company's consolidated financial statements. In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern which requires management to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and provide related footnote disclosures. The guidance is effective for annual or interim reporting periods beginning on or after December 15, 2016. Early adoption is permitted for financial statements that have not been previously issued. The standard allows for either a full retrospective or modified retrospective transition method. The Company does not expect this standard to have an impact on the Company's consolidated financial statements upon adoption.



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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of November 1, 2014, there was no material change in the market risks described in “Quantitative and Qualitative Disclosures About Market Risks” in the Company’s Annual Report on Form 10-K for the fiscal year ended February 1, 2014.

ITEM 4. CONTROLS AND PROCEDURES

At the end of the period covered by this Quarterly Report on Form 10-Q, the Company carried out an evaluation, under the supervision and with the participation of the Company’s Disclosure Committee and management, including the Chief Executive Officer and the Chief Financial Officer of the effectiveness of the design and operation of the Company’s disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures were effective as of November 1, 2014.

There has been no change in our internal control over financial reporting during the most recent fiscal quarter that has materially affected, or that is reasonably likely to materially affect, our internal control over financial reporting.

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## PART II. OTHER INFORMATION

## ITEM 1A. RISK FACTORS

## Risks Related to Our Business

Our inability to predict trends and to respond in a timely manner to changes in consumer demand could adversely affect our net revenues and results of operations.

Our success depends on our ability to gauge the fashion tastes of our customers and to provide merchandise that satisfies consumer demand in a timely manner. Our products must appeal to a broad range of consumers whose preferences cannot be predicted with certainty and are subject to rapid change. We cannot assure you that we will be able to continue to develop appealing products or meet changing consumer demands. If we misjudge the market for our products, including changes to our patterns and our fabrications, revenue may be negatively impacted. In addition, we may be faced with significant excess inventories for some products and missed opportunities for other products. Changes to our product assortment, as well as the availability and breadth of pattern assortment and new fabrications may not gain consumer acceptance. Merchandise misjudgments could adversely impact our net revenues and results of operations.

Additional risk factors have been previously set forth in the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2014.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On September 9, 2014, the Company's board of directors approved a share repurchase program (the "2014 Share Repurchase Program") authorizing up to \$40.0 million of repurchases of shares of the Company's common stock. The 2014 Share Repurchase Program expires in October 2016. During the thirteen weeks ended November 1, 2014, the Company repurchased 168,582 shares of the Company's common stock at an average price of \$20.96 per share, excluding commissions.

Details on the shares repurchased under the program during the thirteen weeks ended November 1, 2014 are as follows:

| Period                                | Total Number of<br>Shares Purchased | Average Price Paid<br>per Share | Total Number of<br>Shares Purchased<br>as Part of Publicly<br>Announced Plans<br>or Programs | Maximum<br>Approximate Dollar<br>Value of Shares that<br>May Yet be<br>Purchased Under<br>the Plans or<br>Program |
|---------------------------------------|-------------------------------------|---------------------------------|--|---|
| August 3, 2014 - August 30, 2014—     |                                     | \$—                             | —  | \$40,000,000  |
| August 31, 2014 - October 4,<br>2014  | —                                   | —                               | —  | 40,000,000  |
| October 5, 2014 - November 1,<br>2014 | 168,582                             | 20.96                           | 168,582  | 36,466,976  |
|                                       | 168,582                             | \$20.96                         | 168,582  |   |

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ITEM 6. EXHIBITS

a. Exhibits

| Exhibit No. | Description                   |
|-------------|-------------------------------|
| 31.1        | CEO Section 302 Certification |
| 31.2        | CFO Section 302 Certification |
| 32.1        | Section 906 Certifications*   |

101 The following materials from the Vera Bradley, Inc.'s Quarterly Report on Form 10-Q for the quarter ended November 1, 2014 formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Statements of Income for the Thirteen and Thirty-Nine Weeks ended November 1, 2014 and November 2, 2013; (ii) Consolidated Statements of Comprehensive Income for the Thirteen and Thirty-Nine Weeks ended November 1, 2014 and November 2, 2013; (iii) Consolidated Balance Sheets as of November 1, 2014 and February 1, 2014; (iv) Consolidated Statements of Cash Flows for the Thirty-Nine Weeks ended November 1, 2014 and November 2, 2013, and (v) Notes to Consolidated Financial Statements. \*\*

\* Furnished, not filed.

\*\* Pursuant to Rule 406T of SEC Regulation S-T, the Interactive Data Files included as Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under these Sections.

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Vera Bradley, Inc.  
(Registrant)

Date: December 10, 2014

/s/ Kevin J. Sierks  
Kevin J. Sierks  
Executive Vice President – Chief Financial Officer

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EXHIBIT INDEX

| Exhibit<br>No. | Description |
|----------------|-------------|
|----------------|-------------|

|      |                               |
|------|-------------------------------|
| 31.1 | CEO Section 302 Certification |
|------|-------------------------------|

|      |                               |
|------|-------------------------------|
| 31.2 | CFO Section 302 Certification |
|------|-------------------------------|

|      |                             |
|------|-----------------------------|
| 32.1 | Section 906 Certifications* |
|------|-----------------------------|

|     |  |
|-----|--|
| 101 | <p>The following materials from the Vera Bradley, Inc.'s Quarterly Report on Form 10-Q for the quarter ended November 1, 2014 formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Statements of Income for the Thirteen and Thirty-Nine Weeks ended November 1, 2014 and November 2, 2013; (ii) Consolidated Statements of Comprehensive Income for the Thirteen and Thirty-Nine Weeks ended November 1, 2014 and November 2, 2013; (iii) Consolidated Balance Sheets as of November 1, 2014 and February 1, 2014; (iv) Consolidated Statements of Cash Flows for the Thirty-Nine Weeks ended November 1, 2014 and November 2, 2013, and (v) Notes to Consolidated Financial Statements. **</p> |
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